Ministry of Planning and Investment (MPI)

Government of Lao PDR

Public Private Partnerships
Frequently Asked Questions

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Governance and Capacity Development in Public Sector Management Program (Public Private Partnerships)

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Quick Reference to Key Questions

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1. Public-Private Partnerships (PPPs) – What are they?

1.1. *What is a Public-Private Partnership (PPP)?*

Basically, a Public-Private Partnership (PPP) is an arrangement between the Government of Lao PDR and a private company for provision of infrastructure and services. More specifically, it is:

- a contract between a Public Agency and a private sector entity (usually of medium or long-term duration) awarded through competition
- where the private partner performs a public function (e.g. provides infrastructure, a service to the public, or both)
- and is allowed to develop the best way of providing the infrastructure or service (so-called 'output specification')
- but where it also carries the risk that if it does not perform well its payments will be affected (so-called 'risk allocation').

Sometimes PPPs are confused with privatization, with Corporate Social Responsibility (where businesses donate funds or resources for a project), or with discussion forums between government and business. To avoid such confusion, the definition above is how PPPs are defined at present in Lao PDR.

1.2. *Are PPPs the same as privatization?*

No. Privatization is the disposal (usually the outright sale) of assets or functions owned by a government that are not considered a core public function of a government. Once the asset or function has been privatized (or sold), the government has no or very limited further formal relationship with the party who bought it.

1.3. *The government of Lao PDR has always hired private companies for construction projects and for supplying equipment and supplies to government. Aren't these also PPPs?*

No. These are mainly short-term contracts where many of the risks remain with the Public Agency. For clarity, the following are not considered PPPs :

- Engineering Procurement Construction (EPC) contracts where the management or operations and maintenance of the asset is not retained by the private sector after three years from completion of construction;
- Supply contracts for goods or services less than three years;
- Rent or lease contracts without any performance obligations and other essential features of a PPP.

1.4. *Are the large hydropower projects realized in Lao PDR in recent years PPP projects?*

Yes. Although they have not been formally introduced to the local market as PPPs, the large hydropower dam transactions recently concluded meet the definition above and can be considered as the only real PPP experience to date in Lao PDR. In the energy sector, PPPs are therefore well established, with private companies providing and selling power to Electricité du Laos (EDL) under IPP arrangements.

These project are relevant examples of PPPs. However the new PPP focus places more emphasis on structuring the projects better and introducing competitive procurement in order to get better performance (measured in value-for-money). It also introduces PPPs for infrastructure and services where charging a user for the service (in this case EDL) is not possible, and where the government itself buys the service. This widens the scope for PPPs to other sectors like social services, government buildings, etc.

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1.5. How are PPPs financed? Where does the money come from?

This is an important question as sometimes people think that PPPs are '*for free*' or '*free money*' – i.e. that a private firm will invest in providing a service without government, taxpayers or users having to pay for it. This is not the case. In a PPP the private partner may provide all or some of the financing needed (for construction, operation and maintenance), but the partner will expect to get its investment back with appropriate profits. The project therefore has to generate enough income to cover all the expenses and the returns needed by the private investor. Income can come from charging users (and government giving up these revenues), by government paying for the service on behalf of users, by commercially exploiting related assets (that could otherwise have been used), or by some combination of these. In all cases someone is having to pay to make the project commercially viable. However a well-structured PPP can usually achieve better value-for-money for user or government payments and clever structuring of commercial exploitation can create a cross-subsidy effect.

2. Who are the 'partners' in PPPs?

2.1. Who are the partners in a PPP?

At the centre of a PPP is a contract signed between a Public Agency (Public Partner) and a private company (Private Partner). The Public Agency is usually the public organization responsible for the infrastructure or services and authorized to sign such a contract.

The private partner is usually a company undertaking the project that signs the contract with the Public Agency. Depending on the project specifics, the private company may also bring in separate companies to do the construction, the operation and the maintenance, and in some cases to provide inputs (e.g. water for a water purification facility or coal for a thermal power station). Depending on the project, there may also be formal arrangements with the users of the service (e.g. for electricity an Agency that buys electricity from a power plant). There are often also insurance companies involved providing insurance, as well as financial institutions (e.g. banks). To organize this, the lead company often sets up a Special Purpose Company (SPC), which is a company whose only objective is to undertake the PPP project. The SPC then enters into agreements with all of the other private partners involved. In some cases there may also be a Regulator involved.

Beyond this group, sometimes also consumer organizations, oversight bodies, NGOs, community groups and other such bodies are mentioned as 'partners', however these partners are usually not part of the core PPP contracts and arrangements.

2.2. What kinds of companies are interested in PPPs?

Often construction companies are first to respond to PPPs announced by government, since they have been doing traditional government construction projects in the past. However companies that operate services (e.g. water companies, power producers, transit operators, etc.) are also keen to respond. As the PPP market develops in a country, it is usual for the local industry to reorganize in response. Specialized project development firms can emerge that are skilled at bringing all the needed partners together to respond to PPP projects. Often construction companies buy up smaller project management firms to enable them to respond to integrated PPP projects.

Foreign firms with more experience with PPP projects are often very important players to bring skills, expertise and technology into the local market.

2.3. Can the private company in a PPP be foreign, or must it be Laotian?

Foreign firms can respond to PPP projects and become partners in a PPP. However the requirements regarding foreign investment in Lao PDR need to be followed.

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2.4. Which kinds of financial institutions and investors are usually interested in PPP projects?

PPP projects are usually financed by a combination of equity (an investor's own money) and debt (money usually borrowed from a bank). Equity is often sourced from the companies taking the lead in the PPP, but can include wealthy individual investors or institutional investors (e.g. pension funds). Institutional investors often like PPP projects as they need large amounts of money to be invested with returns over a long period of time. Such projects suit the investment needs of these institutional investors.

Banks working alone or more commonly together usually provide loans when projects need debt financing. To finance PPPs, bank loans often need to be large and to have long maturity periods. This can be a problem during early stages of a country's PPP market development.

Projects of large investment size often need foreign equity and debt providers, as local investors and banks may not be able to provide sufficient financing at the required terms. Multilateral development banks such as ADB and the World Bank are often especially interested to finance PPP projects, either directly or through guarantees.

3. Why use PPPs?

3.1. What are the benefits of using PPPs?

Well-structured PPPs, where the private partner can determine how a service can best be provided, where risks are well allocated, and where the project is awarded through competitive procurement, can offer better value-for-money than traditional delivery by government. Some of the main benefits private partners can bring are:

- Construction of projects on time and on budget
- Overall more efficient and effective management of the entire project
- Development of more innovative ways of delivering services
- Better use of appropriate technologies
- Lifecycle optimization (better relationship between design and construction, and operation and maintenance over time)
- Better exploitation of direct and secondary project assets
- Private financing
- Better delivery capacity

3.2. PPPs seem to be complicated. Why should Lao PDR consider doing them?

Considering the experience of many other countries, there seem to be three main reasons why Lao PDR should consider PPPs:

- Well-structured PPPs can deliver better value-for-money when delivering services for Lao PDR (better services at a better price)
- PPPs can use private financing to spread the cost of a project over many years, when the government of Lao PDR lacks the budget to do the project now
- Lao PDR is developing rapidly and requires infrastructure and services to support its economy and people. The government of Lao PDR does not have the human and financial capacity alone to deliver and manage all the infrastructure and services required.

3.3. If a project is feasible, why not let the government or a State-Owned Enterprise do it?

By involving a private company the project can often be delivered in a more efficient and cost effective manner than by the government or a State-Owned Enterprise itself. This is because if the PPP is well-structured, the private company

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will find more innovative ways of delivering it, and will usually do the maintenance and operations better and more efficiently. Involving a private partner can also make financing available where public funds are lacking.

There are techniques which can be used (specifically a 'Public Sector Comparator') to assess whether it is better to do the project by government or through a PPP.

3.4. *Why not just take out a 'cheap' government loan and have the government do the project?*

Although the government can almost always borrow money at better rates (more cheaply) than private companies, private companies can almost always design, operate and maintain infrastructure and services better than the government. In well-structured PPPs the additional benefits that private companies bring usually outweigh the cheaper costs of public financing.

3.5. *Will there be competition between infrastructure and services delivered by PPPs and by government agencies?*

There can be. In some cases this competition from other services is very important to create value in a PPP, for instance where alternative routes prevent a toll company from setting toll prices too high.

However, most PPPs require private companies to make significant investments that will take many years to pay off. If the government competes against or undercuts these firms it can seriously undermine their investment and business.

3.6. *Can PPPs solve all the budget shortfalls in Lao PDR?*

PPPs can help the government of Lao PDR to get more services from its budget in a few ways. Well-structured PPPs can deliver services more cost-effectively, they can create value by better exploitation of assets, and they can spread out the budget needs of government by moving financing to the private sector. For example, if a Public Agency does not have the required investment amount in its budget to invest in a new project this year, it could enter into a 15-year contract with a company to finance and provide that project and then the investment amount would be spread over 15 years. But there is a limit to how much this can be done by the government.

PPPs always require sufficient revenues from service users or from government payments to be commercially viable. There is a limit to how much service users can pay and how much the government of Lao PDR can raise through taxes. PPPs can help, but they will not solve all problems.

4. Where can PPPs be used?

4.1. *In what sectors can a PPP be used?*

PPPs are often started first in sectors with revenue streams from users than can be separated, such as toll roads. However, using availability payments (where government 'buys' the services) opens PPPs up in many other sectors. Specific sectors include:

- roads, rail, airports, power and communication;
- health care, education, accommodation, public housing, court and correctional facilities;
- municipal services like water supply, sanitation, garbage collection, sewage disposal, water treatment plants, municipal markets, rural roads and bus stations;
- Industrial infrastructure and related services such as R&D centers, common laboratory and testing facilities for industries, and industrial parks.

Keep in mind that oil and gas projects, mining and telecommunications are mainly private activities and are not considered PPPs.

4.2. Can PPPs be applied in the social sectors?

Yes. It is becoming more common in the social sectors to have the facilities (e.g. school buildings, hospital buildings) developed and managed by private partners, while the public sector focuses on providing the actual service (e.g. teaching, medical treatment). In some cases the actual social service itself can also be provided by private partners as well as the facility.

4.3. What criteria can be used to determine if a project is suitable to be a PPP?

In theory, almost any project could be structured as a PPP. The question is whether it is actually worthwhile making it a PPP. This needs to compare the potential benefits that a PPP arrangement for the project would provide, against the additional costs (e.g. transaction structuring) that would be required to structure it as a PPP. The following criteria can help to guide the decision:

- Project size – in general larger projects may have more opportunities to create PPP value (and offset the higher transaction costs)
- Project duration – projects with longer lifecycles are often more suited for PPPs. However, many smaller PPP projects can have shorter durations
- Complex projects – more complex projects have more opportunities for private sector innovation
- Public alternative – if the government is unable to provide the infrastructure or service itself (for capacity, technical, financial or other reasons), then a PPP may be the only option
- Potential market interest – will private companies be interested and have the skills to take on such a project, either with or without involving foreign companies who may bring more experience?
- Legacy – if other projects for the same or very similar infrastructure or service have been done in Lao PDR before on a PPP basis
- Potential lifecycle integration – projects which can allow the private partner to deal with the infrastructure design, provision, operation and maintenance are more suited for PPPs
- Potential commercial exploitation – projects which have the potential for the generation of other sources of income have more potential as PPPs

4.4. Does a PPP include both the infrastructure and the service?

A PPP can include both the infrastructure (facility) and the service together, or the infrastructure alone, or the service alone. Integrating the infrastructure and the service together can optimize what kind of infrastructure is provided to best suit the service that is to be delivered. If the infrastructure and service are separated, careful attention must be paid to the interface between them. Is it the right infrastructure for the service, and what effect might the service have on the infrastructure?

It is also possible to have one PPP for the provision of the infrastructure and another PPP for the provision of the service. For example, a railway line may be developed and maintained through a PPP based on availability payments by government. The train service might be another PPP with a private operator obtaining revenues from fee paying passengers. Again careful attention is needed to the interface between the two PPPs.

4.5. Could only parts of a service or infrastructure be made into a PPP?

Yes. If it makes sense to have only part of a service or infrastructure delivered by a private party, then there is no reason why this should not be the case. However, always consider that private companies can often create value through better integration such as integration between the infrastructure used and the service to be provided, between the design of facilities and their maintenance over time, etc. Dividing up a service can reduce these integration advantages. Also, dividing up a service can cause interface problems in the connection between what the PPP does and the part of the service or facility that stays under government control.

In some sectors, 'unbundling' is used to divide the whole services into different parts with different forms of PPP in each. A common example is the power sector, where generation of power may be organized through PPPs, while the power transmission lines are managed by the public sector.

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4.6. *Do PPPs always have to be big or mega projects? What about smaller projects?*

Smaller projects may also be suited to PPPs, but as they are smaller it may not be worthwhile to follow the full procedures and arrangements required to structure a large PPP transaction. Smaller projects can therefore be procured following the existing procurement regulations that apply. However, keep in mind that traditional procurement legislation is usually not well suited to procuring PPP projects, as it usually does not allow for negotiation to improve bids and it requires selection of the cheapest financial offer rather than the one offering best value-for-money.

4.7. *Will PPPs only be implemented for the more profitable infrastructure and services?*

PPPs are definitely easier to arrange for infrastructure and services which are more commercially viable and profitable, since less external support is needed. For infrastructure and services which are less profitable, such as social services or services in poor areas, PPPs probably need extra government support to make them viable. This may be done by the government itself by buying the services from the private partner (availability payments), by some form of direct subsidy, or by indirect subsidies by for example allowing the private partner to use commercially viable assets in return for providing the service. Several countries have set up Viability Gap Funds, which are funds the fill the gap between what users can pay and what is needed to make a project commercially viable.

5. How does the government's role change with PPPs?

5.1. *Do PPPs mean the government gives up all its responsibilities for delivering a service to the public?*

No. The Public Agency remains accountable for ensuring the service is delivered. The Public Agency must manage the private partner to make sure the services are delivered satisfactorily. If they are not, the Public Agency is responsible for finding a solution. This is one reason why a Public Agency needs to make sure PPPs and PPP contracts are well structured.

5.2. *Implementing PPPs seems to require a different mindset in public agencies. How should Public Agencies think about their role in service delivery?*

The key question a Public Agency should ask is "what is the most effective way to deliver the infrastructure and services we are responsible for": direct delivery or using a PPP? In both cases the Public Agency remains responsible for making sure the service is delivered, but *how* you do it is quite different. If you use a PPP approach your role will be to structure, procure and monitor delivery of the service, rather than doing it yourself.

5.3. *What happens to PPPs when the government changes?*

PPPs are contracts between the government of Lao PDR and private firms lasting over many years. The binding nature of PPP contracts does not change when the political leadership of government changes. If a new government did decide to terminate a running PPP contract for arbitrary reasons (e.g. purely political), it would encounter a similar response from companies and financial markets as if it defaulted on government debt. Companies and debt providers would immediately see PPP projects as more risky, market response to projects would reduce (or even stop completely), and all private partners would require higher returns to compensate for the risk. In other words all PPP projects would become more expensive and offer less value-for-money.

5.4. *How will my job in government change if we introduce PPPs?*

When a Public Agency moves from directly delivering a service to delivering it using a PPP the role of the Public Agency changes considerably. Instead of direct provider, the role of the Public Agency becomes that of a manager for the delivery of the service by a private company. Staff involved in operating and maintaining the service would no longer be employed by the Public Agency, but by the private partner. The Public Agency will need staff skilled at structuring,

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procuring and managing PPP contracts and arrangements. Typically, the Public Agency will require fewer staff overall, and the staff it needs usually require higher qualifications and management expertise. This can present exciting opportunities for government employees.

5.5. *PPPs seem complicated. Why should a manager in a Public Agency make the effort? What are the incentives?*

There are many incentives for a manager in a Public Agency to consider PPP projects, including:

- It is an important way to get projects delivered, also when budgets are limited
- In the future PPPs will undoubtedly become a major new approach for project delivery in Lao PDR. Being at the forefront of this can be exciting and can improve your skills and experience and position you for future opportunities
- Structuring and procuring PPPs can be intellectually and professionally interesting
- Working on PPP projects can be part of your personal development as a professional and a manager

5.6. *What about the unions?*

Public sector unions can sometimes oppose PPP projects, especially where they believe the PPP may cause job losses or changes in employee conditions. Such concerns of unions are more common for existing (brownfield) projects involving the restructuring of an existing public service into a PPP arrangement, than for completely new (greenfield) projects.

In such cases, good consultation with unions is important. This falls under the mandate of the Ministry or Public Agency for that sector. Many concerns raised by unions can be addressed through how a PPP is structured, provisions for the transfer of workers to the new company, and so on.

5.7. *How can the government of Lao PDR get staff skilled in structuring and implementing PPPs? Or must we always use consultants?*

The best way to develop the PPP skills of staff is to actually implement PPP projects. It is very common to also use specialized technical, financial, legal and procurement consultants for PPP projects, since they bring in highly specialized (and expensive) skills that the government does not need to have all the time.

5.8. *If a PPP project is profitable, should the government have a share of the profits?*

PPPs need to be profitable to the private partner or they will not invest in and do them. The government and users benefit from this by getting better value-for-money in the services delivered. A profitable project should not be a concern. If the PPP is structured well and risks are allocated properly, the private partner should achieve a reasonable profit if it performs well, and the services should indeed be better value-for-money.

It can happen however that for some reason a PPP project becomes 'super profitable', where the private partner has profits far above what can be expected for a project of that nature and risk profile. If a Public Agency is concerned this might happen it can include a 'benefit share' provision in the PPP contract, in which profits above a set level are shared with government.

5.9. *How can the government of Lao PDR develop the private market for PPP projects?*

The single most important requirement to establish a strong PPP market is to bring a pipeline of well-structured PPP projects to the market. Also important are the following:

- Foster market certainty and clarity
- Demonstrating top political support of the government of Lao PDR to PPPs
- Make sure the policy and legal framework is in place
- Remaining consistent in the PPP approach and not making ad hoc changes to policies or to projects

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- Where necessary provide support and enhancements to make projects viable
- Clearly communicate the government of Lao PDR's infrastructure and service plans to the market

6. Key ingredients for creating PPP value

6.1. *What is lifecycle optimization and why is it important in a PPP?*

Lifecycle optimization means the relationship between how something is designed and built today, and how much it costs to operate and maintain over its working life. Cheap construction may mean heavy maintenance costs and disrupted operations in later years, but too expensive construction can be wasted as it may be higher than what is actually required to do the job. Private companies are good at getting this balance right (lifecycle optimization) when their profitability is affected by design, construction, operations and maintenance over the project lifecycle.

6.2. *How long should the contract period of a PPP be?*

This should be worked out for each project based on technical and financial analysis. Generally, the duration of a PPP contract is linked to the lifespan of the main facilities or assets involved. The contract often lasts until the facility or asset has to be replaced. But contract duration also needs to take into account how long the private party needs to get their investment back with a reasonable return on investment. So the duration will be affected by the investment size, whether this is all privately financed, and the revenues for the project.

6.3. *What are some of the main things to consider to make sure PPPs create better value than public/government provision?*

Four issues are especially important:

- Output Specification – this allows for private innovation
- Risk Allocation – this creates the incentive framework for better private performance
- Competitive Procurement – this makes companies compete to offer the best deal
- Post-Contract Management – the value created by a PPP is realized when it is actually implemented

6.4. *What is 'output specification' and why should we define the outputs we need, rather than the inputs?*

An Output Specification focuses on the desired outputs of a service, rather than a detailed technical specification of how the service should be provided. This lets the private partner develop and propose innovative solutions for providing the service. If an Input Specification is used in which all the details of facilities, equipment, procedures and so on are specified by government, then the private partner does not have much room to innovate and improve.

6.5. *Why is risk allocation important in PPPs?*

Allocating risks between partners is one of the most important ways to create value with PPPs. When a partner is made responsible for a particular PPP project risk then it will do whatever it can to make sure that the risk does not occur. For example, if the private partner is responsible for the risk that a facility is not built on time (e.g. it must pay a fine for delays, or it cannot charge users until the facility is ready), then it will do everything to make sure the facility is ready on time. This is what creates an incentive for more efficiency.

But risks are transferred between partners at a price. If the public partner allocates a risk to the private partner, the private partner will need more payment to cover this extra risk. So risk transfer only works when the performance incentive it creates is worth more than the extra cost charged for the risk. This happens when the risk is given to the partner who can manage that risk best and at the lowest cost. Some risks are best treated by sharing them between the partners.

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Practically, PPP risks are defined in a risk matrix (a table on which all risks are identified and it is indicated to which partner each risk is allocated). Then this is translated into how the project is structured, into the financial, payment and monitoring/penalty arrangements, and into the PPP contract.

6.6. *Some government staff think that if the private sector wants to be involved, then it should be prepared to take all the risks. Is this right?*

No. If you transfer a risk to a private partner that it cannot manage well itself , it will need to have a very high financial reward in return (in other words the price of the PPP for the government will go up). This can make a PPP project so risky for a private partner that none will be interested, or it can simply make the project so expensive for government that it is not worthwhile.

Do note that risk allocation in PPP projects is also sensitive to the stage of the PPP market in a country. Typically in earlier stages when PPP projects are new to private partners the government may have to carry a bit more risk to support deal flow than can be achieved in projects as the market matures.

6.7. *What role does competition play when appointing the private partner? Is it important to have competitive procurement or can we just negotiate with one private partner?*

Competition is absolutely crucial in the sense that it drives firms to perform better and results in better prices. Having competitive procurement – i.e. companies competing against each other – for the selection of a private partner is a key value driver, and is most intense during the formal procurement process of the project. This is a unique moment in which the government can create significant value.

When a private partner is selected and the PPP awarded, the government can still use competition indirectly by the threat of replacement of the private partner if it does not perform adequately. In some cases it is possible to have competition from alternative service providers or services as a way to keep competitive forces ongoing.

7. Responsibilities and procedures

7.1. *Who can initiate a PPP project?*

PPPs can be initiated by National Government, Local Governments, State-Owned Enterprises, Local Authorities, Government Agencies or any other Government Unit. These are known as the Public Agency.

PPPs can also be initiated by a private company that submits an unsolicited proposal to the government.

7.2. *What are the main steps or stages in establishing a PPP contract?*

The main steps in establishing a PPP project are:

1. Preliminary Study – in which the initial project idea is worked out
2. Feasibility Study – in which the project is assessed and developed in more detail and the tender documents are developed
3. Tender Process – in which the PPP project is competitively procured and awarded
4. Contract Management – in which the awarded contract is implemented and managed

7.3. *How long does a PPP transaction take?*

PPPs usually take longer to structure and procure than traditional project procurements. It also depends on how complicated the project is, and how experienced the Public Agency, its advisors and the private bidders are at such projects. Typically, structuring a PPP can take anywhere from 2 to 12 months, depending on how complex the project is. It is usually necessary to test the project with the market and build market interest. The formal procurement typically takes between 6 and 12 months to complete to financial close.

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7.4. Which regulations / procedures should be followed for procuring PPP projects?

Projects that meet the definition of PPPs must follow PPP procurement regulations and procedures. These regulations and procedures are still being developed in Lao PDR.

7.5. What are the roles when procuring / approving PPPs?

The institutional framework for developing PPPs in Lao PDR is still being developed.

Generally speaking the central role of identifying, developing, procuring and managing a PPP project belongs to Project Agencies (a Department or equivalent, State-Owned Enterprise, State Agency or local administration owning the project). Support, supervision and where relevant approval of PPP projects undertaken by Public Agencies is the role of the Ministry concerned, the Council of Ministers (for large and/or strategic projects), the Ministry of Finance (for projects involving existing assets) and the Ministry of Planning and Investment (for new projects). A Selection Committee has the role of evaluating PPP proposals and recommending the winner to the Responsible Minister and Council of Ministers. The Council of Ministers is responsible for final decision-making on the award of PPP projects.

7.6. PPP procurement may require some negotiation with private bidders to improve their bids. How can officials manage this, and how can they avoid being accused of corruption?

Negotiation between the public partner and private parties does indeed have a place in good PPP procurement. In Europe, there is a formal 'competitive dialogue' procedure which can be used early on in the procurement process if the public partner wants private parties to contribute to how the project is structured and specified. Generally, PPP procurement procedures allow the public agency to ask bidders to clarify their submitted proposals, and to improve them, before making a final selection. This is important to maximize the value-for-money of bids.

If the Selection Committee and officials follow the relevant procurement procedures correctly and undertake any negotiations in a well-recorded, transparent and competitive manner, the process will be fair and defendable.

8. Deciding whether to award a PPP

8.1. If I am procuring a PPP project, how do I know which offer is the best for the government and taxpayers?

Traditional government procurement usually awards the contract to the compliant offer with the least expensive bid. When dealing with PPPs, the concept of value-for-money is usually used instead of the lowest bid price. The compliant proposal that offers the best value-for-money should be selected. It is possible to still use a Least Cost approach to evaluating PPPs, but the evaluation needs to be set up accordingly to make sure quality/quantity and risk are duly considered.

8.2. What is value-for-money?

Value-for-money means the relationship between the quality and/or quantity of service provided, the risk for government, and the price of a PPP project. When these factors are combined, the best combination can be identified – offering the best value-for-money.

8.3. When and how is the value-for-money of a PPP determined?

The value-for-money of a PPP can be estimated before the procurement process when the Public Agency needs to decide whether to deliver the project as a PPP or through traditional procurement. At this stage the value-for-money can be estimated using a Public Sector Comparator Model. This is a financial model which compares how much it would

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cost to deliver the project as a traditional government project and how much as a PPP project. The model includes all the direct project costs and revenues, as well as the costs of the project risks.

Later in the procurement process, value-for-money assessment is used to for evaluating proposals submitted by private bidders. Here a PPP Reference Model is used, which is a financial model of what a private offer for the project can be expected to be. The submitted bids are compared against this taking quality/quantity, risk and price into account.

8.4. Who checks whether a PPP delivers value-for-money or not?

This is the responsibility of the Public Agency doing the PPP project and the project Selection Committee. Keep in mind that value-for-money is an important, but not the only consideration when evaluating a PPP. Evaluators should also consider things like the capacity to implement the project, the effect the contract may have on the budget, implications for service users and the public, etc.

8.5. What is a Public Sector Comparator (PSC) Model? When do I use it and for what purposes?

The PSC is a financial model, usually made in MS Excel. It is an estimate of how much it would cost for the government of Lao PDR to deliver the project itself, over the whole lifetime of the project, and including the costs of all project risks the government would have. You can then make adjustments to compare how much it would cost if the project was delivered as a PPP. This can be used as one factor to consider when deciding at an early stage whether to carry on with the project as a PPP or not. The PSC can be further developed and used later to compare the actual proposals submitted by private partners during the formal procurement process. This gives the Public Agency a benchmark against which to assess and compare the bids received.

9. PPPs and the Budget

9.1. What does signing a PPP project mean for the budget of the Public Agency concerned?

The effect on the Public Agency's budget depends on what kind of PPP project it is. There can be many considerations and adjustments, including:

- For PPP projects where the government pays an Availability Payment or subsidy to the private partner, the Public Agency needs to enter these payments into their annual budget, and also plan them into budget years
- For PPP projects where the private partner collects revenue themselves from users, the Public Agency may need to remove these revenues from their budget if they were collecting them previously. If the private partner will pay a concession or similar fee to government, this revenue should be added to the budget
- For all forms of PPPs, the Public Agency will need to budget for the staff and expenditure needed to manage and monitor the PPP
- If the Public Agency is replacing a project it was going to do itself with a PPP, it may need to remove the related capital spending from its budget, and possibly replace this with an annual Availability Payment
- If the PPP involves a function currently being done by the Public Agency being transferred to a PPP, then the related staff and other costs may need to be removed from the Public Agency budget, although any costs related to this should also be considered
- The Public Agency also needs to consider the risks related to the PPP that it carries. If it is considered likely that one of these risks may happen, then the Public Agency should already add this to its budget. Other risks which might occur (but which are less likely) should be noted, but do not need to be specifically budgeted for.

So when doing a PPP the Public Agency should carefully analyze how it will affect its budget and what changes need to be made. It is especially important to assess whether the PPP will be affordable to the Public Agency over its project life. The Ministry of Finance should be consulted regarding this.

9.2. *Should risks and contingent liabilities be included in the budget?*

The risks that the government retains or shares when a PPP project is awarded should be clearly identified and transparently recorded. The Public Agency should consider how each of these risks can best be managed, and should identify and take whatever measures it can to manage them. It is also good practice to identify who is responsible in the Public Agency for monitoring and managing each risk.

When the Public Agency considers that a risk is very likely to happen in any year, then it should add a provision in the budget for that risk. Risks that are not considered likely to occur need to always be transparently recorded, but specific budget provision does not need to be made.

9.3. *Can the government of Lao PDR provide guarantees or other support for PPP projects?*

Some PPP projects do require additional support to be commercially viable or bankable. Especially for initial projects when PPP projects are less familiar in Lao PDR, it may be necessary to provide additional support. Government support for a PPP project can be direct, such as structuring the project with Availability Payments or with a partial subsidy, or it can be indirect by providing for example some form of guarantee to the private partner or its financiers.

It is crucial that the Public Agency considers very carefully what effects any support it gives will have on the risk structure of the PPP project and on the private partner's incentives and performance. Also, the budgetary impacts and affordability of support needs to be assessed. The Ministry of Finance needs to be closely consulted and must authorize any such support.

10. Managing Private Partners

10.1. *How can we ensure that the private partner performs properly?*

There are a few things that can be done:

- Choose a good private partner in the first place, use competitive procurement, and make sure to pre-qualify firms that have the capacity to do the project
- Establish a good and fair working relationship between the public and the private partner
- Make sure risks are allocated well in the PPP, putting the private partner under the right incentives to perform
- Build performance monitoring and checks into the PPP contract, and make sure that the government regularly, properly and fairly monitors performance and manages the contract
- Where applicable, provide mechanisms for users of the infrastructure or service to provide feedback
- Make sure there are appropriate mechanisms and penalties in place to correct under-performance by the private partner
- Keep in mind that if banks are providing project-based loans to the private partner, then the banks will also check on the performance of the borrower

10.2. *What happens if the private partner fails to perform?*

The collapse of a PPP agreement or the default of a private partner can be very messy and costly and generally benefits no one. The allocation of specific risks to the private partner in a PPP ensures that good performance is encouraged. A well-structured PPP contract should lay out clearly how the performance of the private partner will be monitored, and what actions will be taken if the performance is not adequate. It is a good idea to follow the 'tickle-hurt-kill' approach – have provisions for light penalties or warnings when underperformance first occurs ('tickle'), with increasing measures and penalties if performance is not improved ('hurt'), and with default procedures only where all other measures to improve performance have not worked ('kill').

10.3. Since PPP projects are long-term contracts, are they still flexible if changes occur or are required in the future?

Specific provisions should be included in the PPP contract covering how such future issues should be dealt with. Also make sure that a positive working relationship is maintained between the government and the private partner throughout the implementation period. This makes it easier to discuss any changes which may need to be made.

10.4. What happens when a PPP contract gets to the end of the contract period?

The PPP contract will have provisions explaining precisely what happens when the end of the contract period is reached. Often the PPP contract period is the same as the lifespan of the related infrastructure, so it is common that a new PPP is launched to replace or rehabilitate the infrastructure and run it in the future.

11. Getting Started with PPPs

11.1. It seems PPPs are inevitable to deliver all the infrastructure and services Lao PDR needs. The question seems how we can properly arrange all the PPP projects we need?

Adequate laws and regulations aimed at developing the PPP market in Lao PDR are currently being developed in close cooperation with relevant Ministries and government bodies.

At this point in time the key task for Public Agencies is to actively identify potential PPP projects. Seek support for how such projects can be structured and procured as PPP projects. The only way to get PPP projects done is to actually implement them!

11.2. How can we in a Public Agency take the first steps to formulate a PPP project?

There is no single, prescribed route to follow for the initial stages. Depending on your situation, the following can be useful steps to take:

- Read over this PPP FAQ and browse over the ADB resource materials: PPP Volumes I, II and III
- All PPPs need champions and drivers, so consider forming a team within your Public Agency comprising persons with the right skills and interest to take forward PPPs
- Consider preparing an outline 'Sector Note' on how PPPs could be introduced in your sector or the particular infrastructure or service you are concerned about. This can be a basis to have discussions within your own agency about possible projects and how to proceed. MPI can also assist with identifying the right opportunities
- If you already have a specific PPP project in mind, prepare a project 'Concept Note'. Again this is a basis for discussion in your agency. Contact MPI who can advise you on which other agencies should be consulted
- Contact MPI regarding both the sectoral application of PPPs and particular PPP project ideas. MPI can advise you on further consultations that may be required, and how to get internal and potentially external support to further develop your PPP initiatives
- When your PPP concepts are more formulated and you wish to proceed further, MPI can also advise you on what formal steps need to be taken to further develop your projects

11.3. Do I need consultants to help me do a PPP project?

The Public Agency should appoint a senior official as Project Manager for a PPP transaction supported by a staff team. It is usually advisable that the Project Manager uses external consultants for various parts of structuring and procuring PPP projects. This is because often quite specialized technical, financial, legal and procurement expertise is needed which may not be available in your Agency.

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11.4. What kinds of consultants should I use to structure and procure a PPP project?

It is common for PPP transaction advisors to be appointed to assist with PPP transactions, especially for large, complex or first-time projects. Consultants commonly used for PPPs are:

- Technical advisors – to assist with technical aspects and especially output specifications, as well as environmental and social impact issues
- Legal advisors – for advising on the legal basis for the PPP and for drafting PPP contracts
- Financial advisors – for financial structuring, preparing financial models (e.g. PSC), and evaluating value-for-money of proposals
- Procurement advisors – to advise on the best procurement route and procedures, evaluation criteria, etc.
- Marketing / communication advisors – for large or complex projects it is sometime needed to have significant marketing and communication activities

Make sure the consultants you appoint have proven experience and expertise to properly support you.

11.5. What support is available?

Public Agencies interested to take forward PPP initiatives and projects may contact MPI to identify adequate support.

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12. Glossary of Common PPP Terms

Availability Payment	A regular payment made by the government to a private partner in a PPP provided the private partner provides the required infrastructure and/or service at the required level. Availability Payments can be used instead of the private partner in a PPP collecting revenues directly from the infrastructure or services users. Availability Payments usually include penalties if the infrastructure or service is not available at the required level
Least Cost Approach	A traditional procurement approach where projects are awarded to the qualifying bidder that offers the lowest price. The Least Cost approach can still be used for PPPs, however the evaluation of bids then needs to be designed to ensure that the quality and risk of bids are also taken into account
Output Specification	Defining what is required from a project (infrastructure and/or service) as an output (what), and not as an input (how). Defining projects as outputs lets private partners develop and innovate the best way of achieving those outputs
Public Agency	A Ministry, Agency or State-Owned Enterprise of the government of Lao PDR
Public Sector Comparator	A financial model used to compare the value-for-money of delivering a project as a PPP or as a traditional government project
Risk Allocation	Defining the risks related to a project and giving responsibility for each risk either to the private partner, the public partner or sharing the risk between them. How each risk is allocated effects how the partners are incentivized to perform
Transaction Project Manager	The person/s appointed by a Public Agency to manage and conduct a PPP transaction
Value-for-money	The way in which what a PPP offers to the government or service users is measured, often in comparison to the government doing the project in the traditional way. The value-for-money calculation includes the quality, risk allocation and price of the project
Whole Life Project Costing	Looking at all the costs and revenues of a project over its whole operating life, not just at what the initial capital costs of the project are. This approach is very important for PPPs as it focuses on how a project can be optimally delivered

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